

Revenue
New Issue

San Antonio, Texas

Rating

Municipal Drainage Utility System
Revenue Bonds, Series 2003 A+

Analysts

Jose A. Hernandez
1 512 322-5317
jose.hernandez@fitchratings.com

Jose L. Acosta
1 512 322-5324
jose.acosta@fitchratings.com

Issuer Contact

Milo Nitschke
Director of Finance
1 210 207-8620
milon@sanantonio.gov

New Issue Details

\$43,695,000 Municipal Drainage Utility System Revenue Bonds, Series 2003, are scheduled to sell on April 29 via negotiation to a syndicate managed by Siebert Brandford Shank. Dated May 1, 2003, the bonds will mature serially Feb. 1, 2004–2028. Bonds maturing on or after Feb. 1, 2014 are subject to optional redemption at par plus accrued interest on Feb. 1, 2013 or any date thereafter.

Purpose: Bond proceeds will finance the cost of drainage improvements, including acquisition, construction, and repair of structures, equipment, and facilities for the system.

■ Outlook

The 'A+' rating reflects San Antonio's sound projected debt service coverage, strong stormwater fee collections profile, and anticipated stormwater fund balance increases. Also considered are the adequate legal provisions, including a lenient reserve requirement, and the expectation of limited future borrowing without corresponding increases in the stormwater fee. With the adoption of the fiscal 2003 budget, the stormwater drainage service fee was increased by 30% to accommodate the debt service on this issue, as well as provide for some operational improvements. Through the fee increase and implementation of operational efficiencies, the fund balance for stormwater operations is expected to increase by more than \$3.7 million by the end of fiscal 2003. This will provide sufficient liquidity if the need arises. Also, the fee is collected along with the water and wastewater fees and is based on type of customer and lot size, resulting in a very reliable revenue stream.

■ Rating Considerations

The stormwater system was created in 1997 as a public utility to provide the city with a funding source to comply with federal Environmental Protection Agency-mandated stormwater and operation and maintenance (O&M) requirements. Operational functions include vegetation control, river maintenance, street sweeping, and tunnel maintenance. The operating budget for fiscal 2003 is \$16.7 million, and the appropriation for system transfers to the general fund is about \$1.3 million.

The fee increase is projected to raise \$5 million in revenue, 60% of which will be used for debt service, with the remainder dedicated to operational improvements. The budgeted fund balance is expected to increase from approximately \$100,000 to just over \$3.8 million at the end of fiscal 2003. Using fiscal 2003 budgeted revenues and expenditures, net revenues provide 1.3 times (x) coverage of maximum annual debt service (MADS). Level debt service is anticipated throughout the life of this issue, with only one interest payment in this fiscal year, providing the opportunity to raise the fund balance. Fiscal 2003 gross revenues provide 7.3x coverage of MADS. Development impact fees are also collected; however, they are segregated in a separate fund and used primarily for capital projects.

The city is a partner in an interlocal agreement for a regional flood control program, along with Bexar County and the San Antonio River Authority. The purpose of the agreement is to collaborate with municipalities, military bases, and local, regional, state, and federal agencies to provide regional management of a unified flood control, drainage, and stormwater quality program. As part of the alliance, responsibilities of each partner are still being formulated, including capital project funding. The regional capital improvement plan (CIP) will prioritize projects based on benefits, available funding, and equity. Additionally, the city has

April 28, 2003

commenced planning for its next general obligation debt referendum, which contemplates the possibility of funding drainage projects, similar to past practice. The city's six-year CIP identifies \$56.5 million in drainage projects, none of which contemplate funding through this issue but will rely on proceeds from past tax-supported bond sales. City officials have stated that any future drainage utility system revenue debt issues of any consequence will be accompanied by a corresponding fee increase.

Through an interlocal contract, the San Antonio Water System (SAWS) bills and collects the stormwater drainage fee on behalf of the city. Each property that receives a water service bill also receives a drainage bill. Approximately 90% of all SAWS customers are residential. Residential customers pay either \$27 or \$35.76 annually for drainage service, depending on lot size. Given this low annual charge, rate flexibility for future needs is also a positive rating factor.

Security provisions include a rate covenant that will produce revenues equal to 1.25x annual debt service, O&M expenses, and any other indebtedness payable from pledged revenues. The additional bonds test calls for revenues for the last completed fiscal year or 12 consecutive months out of the immediately preceding 18 months to be at least equal to average annual debt service (AADS). The flow of funds, in priority order, is to debt service, O&M expenses, the reserve requirement, and then any lawful purpose. The reserve requirement is AADS; however, the requirement is waived in each year revenues are at least 1.75x AADS. The city also covenants to discontinue water and sewer services to any user that is delinquent in the payment of drainage charges.

■ Strengths

- Stable revenue stream that will grow steadily and is not likely to fluctuate.
- Low drainage service fee, which allows for future rate increases if needed.
- Sound liquidity level anticipated in the stormwater fund at the end of fiscal 2003.
- No significant additional leveraging of the drainage fee expected without corresponding rate increases.

■ Risks

- Undetermined level of drainage capital needs and city responsibility associated with regional flood control plan.

- Debt service reserve requirement waiver as long as revenues equal 1.75x AADS.

■ Security Provisions

The bonds are special obligations of the system payable solely from and secured by a first lien on and pledge of revenues of the system. The city covenants to discontinue water and sewer services to any user that is delinquent in the payment of drainage charges.

Pledged Revenues: First lien on revenues derived from the operation and ownership of the municipal drainage system, including interest income on accounts.

Rate Covenant: The city stipulates and agrees to establish, maintain, and impose charges for facilities and services reasonably expected to produce revenues sufficient to pay parity debt service and fund reserve requirements, O&M expenses, and an amount equal to 1.25x AADS requirements on parity debt, as well as to pay all other indebtedness payable from and secured by pledged revenues.

Additional Bonds: Additional bonds are authorized subject to a certification from the director or city manager that the city is not in default as to any covenant, obligation, or agreement and all payments into special funds maintained for payment and security of parity obligations have been made. Additionally, revenues for the last completed fiscal year or 12 consecutive months out of the 18 months immediately preceding the issuance of additional bonds must be at least equal to 1.25x AADS. A change in charges for services effective for at least 60 days prior to the last day of the period for which revenues are determined may be considered in the test calculation. Also, obligations payable from and secured by a lien on and pledge of net revenues of the system, junior and subordinate to prior lien obligations, are authorized.

Flow of Funds: In priority order, all revenues deposited into the system fund are pledged and appropriated to debt service payments, O&M expenses, amounts required to be in the reserve, and any lawful purpose, including transfer to the city's general fund.

Reserve Requirement: The reserve amount must equal AADS, funded in monthly installments in an amount equal to at least $\frac{1}{60}$ of the requirement. The reserve requirement is waived for each fiscal year that revenues are at least equal to 1.75x AADS.

Should revenues be less than this threshold, the reserve requirement must be fully funded within two years.

■ Municipal Drainage Utility System

The system serves the city's boundaries and its unincorporated extraterritorial jurisdiction. As a public utility, the city may bill for drainage services along with other municipal utility billings. The stormwater drainage fee is a separate charge against lots and tracts of property that benefit from services. The system is a special revenue fund that provides for the O&M requirements of the city. The rate increase was passed to provide funding for capital projects and operational improvements.

Through an interlocal contract, the fee is collected monthly by SAWS from its customers based on the square footage of the lot or tract and the customer class according to a fee schedule. SAWS is the predominant water service provider in Bexar County, serving more than 306,900 customers representing more than 80% of the water utility customers in the county. SAWS is then reimbursed for its expenses associated with billing, collecting, and accounting. There are four categories of customer classes, with varying tier levels within each class. Customer classes include residential, multifamily, commercial, and public. Future rate increases will be dependent on the levels of revenue debt project financing, pay-as-you-go project funding, and O&M requirements.

Copyright © 2003 by Fitch, Inc., Fitch Ratings Ltd. and its subsidiaries. One State Street Plaza, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. All of the information contained herein is based on information obtained from issuers, other obligors, underwriters, and other sources which Fitch believes to be reliable. Fitch does not audit or verify the truth or accuracy of any such information. As a result, the information in this report is provided "as is" without any representation or warranty of any kind. A Fitch rating is an opinion as to the creditworthiness of a security. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed, suspended, or withdrawn at anytime for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of Great Britain, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.



SAN ANTONIO (CITY OF) TX Muni Drnge Util Sys

Contacts

Kristin Button	214-220-4383
Douglas Benton	214-220-4381

Moody's Rating

Issue	Rating
Municipal Drainage Utility System Revenue Bonds, Series 2003	A1
Sale Amount	\$43,695,000
Expected Sale Date	04/29/03
Rating Description	REVENUE

Moody's Assigns Initial A1 Rating to the City of San Antonio's Municipal Drainage Utility System Revenue Bonds, Series 2003

Rating Affects \$43.6 Million in Debt

Opinion

Moody's Investors Service has assigned an initial A1 rating to the upcoming sale of \$43.6 million City of San Antonio (TX) Municipal Drainage Utility System Revenue Bonds, Series 2003. The current issue will be the only outstanding debt of the system. The rating assignment is based on the strong gross revenue pledge and ample debt service coverage levels supported by satisfactory financial performance. The rating also takes into consideration the System's sizable and diverse service area.

In 1997 the city created this utility system in order to address drainage problems throughout the city. State legislation, enacted in 1989, allows cities to establish municipal drainage utility systems to better manage storm water challenges. Under the statute, the drainage utility system functions similar to that of a city water and sewer utility, by assessing a charge to property owners for drainage. The revenue can be used to maintain drainage ways, to pay for drainage capital projects and to pay for environmental regulations regarding drainage and storm water management. The creation of the drainage utility system as well as the issuance of debt results from the need to address drainage concerns throughout the city.

The City currently assesses two drainage fees. The first is a fee in lieu of detention pond, which is a one-time assessment levied against developers of land and assessed and collected by the City. The fee is determined by acreage and property use according to a set fee schedule. The second fee is a stormwater drainage fee collected monthly by the City's water and sewer system (SAWS) from its customers. Security on the debt is provided by a gross pledge of these revenue sources whereby the flow of funds is for debt service, operations and maintenance and then to the reserve fund. A gross revenue

pledge adds strength to the credit quality of the bonds compared to using net revenues, which is generally considered a weaker pledge. The additional bonds test and rate covenant are satisfactory at 1.25 times the annual debt service requirement.

Drainage fee revenues have grown an average of 4% annually over the last five years as new residential and commercial construction continues with these revenues providing solid coverage of debt service requirements. Fiscal years 2001 and 2002 gross pledged revenues provided debt service coverage of 5.68 times and 5.85 respectively using the 2004 debt payment. Projections for fiscal years 2003 through 2007 indicate debt service coverage will exceed 7.0 times coverage given a 30% increase in the stormwater drainage fee which became effective October of 2002. This increase allows the system to continue supporting operations and pay-go capital improvements. Plans for future debt issuance is modest as the commitment of the system's revenues to pay-go capital improvements will result in low leverage of the system in the foreseeable future. Payout on the issue is slow with only 27% of debt retired in ten years; however, consistent with the projected life of the projects, all debt matures by 2028.

The strength of the service area is reflected in the sizable and diverse tax base of \$40 billion for the City of San Antonio (Moody's rated Aa2). The tax base has grown an average of 6.8% annually for the last five years. SAWS (Moody's rated Aa3) provides water and wastewater services to approximately 1 million people in and around Bexar County (Moody's rated Aa2). By the year 2050, SAWS service area is expected to grow to 2.2 million people and its water demand is expected to double over that same time.

KEY STATISTICS

Fiscal 2002 debt service coverage: 5.85x

Payout of principal (10 years): 27.6%

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY COPYRIGHT LAW AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT. All information contained herein is obtained by **MOODY'S** from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, such information is provided "as is" without warranty of any kind and **MOODY'S**, in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability or fitness for any particular purpose of any such information. Under no circumstances shall **MOODY'S** have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of **MOODY'S** or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if **MOODY'S** is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The credit ratings, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. **NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.** Each rating or other opinion must be weighed solely as one factor in any investment decision made by or on behalf of any user of the information contained herein, and each such user must accordingly make its own study and evaluation of each security and of each issuer and guarantor of, and each provider of credit support for, each security that it may consider purchasing, holding or selling. Pursuant to Section 17(b) of the Securities Act of 1933, **MOODY'S** hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by **MOODY'S** have, prior to assignment of any rating, agreed to pay to **MOODY'S** for appraisal and rating services rendered by it fees ranging from \$1,500 to \$1,500,000.

Publication date: 25-Apr-2003
Reprinted from RatingsDirect

City of San Antonio, Texas; Municipal Drainage Utility System Revenue Bonds, Series 2003

Credit Analysts: Theodore Chapman, Dallas (1) 214-871-1401; James Breeding, Dallas (1) 214-871-1407

Credit Profile

\$43.695 mil Muni Drain Util
Sys Rev Bonds
Series 2003 dtd 05/01/2003
due 02/01/2028
AA-
Sale date: 29-APR-2003

OUTLOOK:
STABLE

Rationale

The 'AA-' rating on San Antonio, Texas' municipal drainage utility system revenue bonds reflects the system's:

- Broad, diversified, and growing service area;
- Sound financial performance over the past several years;
- Demonstrated willingness to adjust rates, although overall rates remain low; and
- Economies of scale in the implementation of some functions of the drainage utility in conjunction with San Antonio Water System (SAWS) ('AA-' senior-lien revenue bond rating).

The San Antonio MSA's average wealth and income levels moderate these strengths.

A first lien gross revenue pledge on the storm water system secures the bonds, the proceeds of which will be used to fund improvements and extensions to the existing system. A debt service reserve in the amount of average annual debt service provides additional security, although the reserve does not have to be funded as long as annual debt service coverage (DSC) remains at least 1.75x. While the rate covenant is a moderate 1.25x average annual debt service, annual DSC is projected to be significantly higher.

Located in Bexar County, about 75 miles south of Austin, Texas, the San Antonio MSA has a population of 1.3 million, making it one of the nation's 10 leading MSAs. Despite a slowing in the 2003 total assessed value (AV) growth to 3.1% from the 7.0% average of the previous five years, overall economic growth continues. Total AV is now almost \$41 billion. The services and trade sectors continue to experience the strongest growth. Medical and biomedical industries account for the largest part of the city's economy, contributing \$8.1 billion to the area as a whole. Expansions continue at South Texas Medical Center, which is the city's leading employer with almost 26,000 employees. Government, specifically the military, remains a large component of the economy with five military bases in the city. Officially, Kelly Air Force Base closed as a military installation in July 2001; the city, however, continues to work on its privatization efforts at the base, which have, so far, resulted in a slight net gain of jobs. The city also worked with Brooks Air Force Base to create Brooks City-Base, which is a collaborative effort between the city and the U.S. Air Force; the city base was established to retain jobs at Brooks by improving the facility's effectiveness. Unemployment in San Antonio has risen to 5.2%; unemployment, however, remains below state and national levels. Overall, median household income levels remain just under state and national averages.

The storm water fund's financial position remains sound. Service rates are low, remaining below \$3 per month for residential services even after a 30% rate increase in 2002. Based on audited 2002 results, maximum annual DSC is projected at 5.8x. Furthermore, liquidity was good with about 260 days' unrestricted cash and equivalents on hand in 2002. Although the responsibilities for the storm water system ultimately rest with the city ('AA+' GO debt rating), SAWS provides some services as part of an interlocal agreement, including monitoring and customer billing. Because the storm water fee is included in the water and sewer bill, collection rates are extremely high.

Outlook

The stable outlook reflects the expectation that the rate structure will generate sufficient revenues for the city to meet its debt service and operational requirements and that any future debt will be manageable.

The Drainage Utility

San Antonio established the drainage utility as a special revenue fund in fiscal 1998. SAWS and the Texas Department of Transportation's San Antonio regional office, as copermittees under the National Pollution Discharge Elimination System, are responsible for storm water runoff management and quality control. While the ultimate responsibility of the drainage utility rests with the city, including rate-setting authority, economies of scale are realized by SAWS performing such functions as testing and monitoring, billing, and inspections. The city reimburses SAWS for any costs incurred by SAWS in the course of its responsibilities, although the revenue stream generated by the drainage utility may only be pledged to the drainage utility's debt. To further offset some growth-related capital costs, the drainage utility also established a fee in lieu of detention pond, which is akin to an impact fee, levied against land developers. The combined revenues generated by the drainage utility have allowed it to fund about \$16 million of drainage improvements annually, although such costs are subordinate to debt service on these and any future parity bonds. Additional bonds may be issued with at least 1.25x average annual DSC, although any additional near-term debt should be manageable given the utility's healthy financial condition.

San Antonio Economy

San Antonio is in south-central Texas. According to the 2000 U.S. Census, San Antonio is the eighth largest city in the nation and the third largest in Texas. Although military and tourism have long been the driving forces in the city's economy, medical and biomedical companies are now the leading force, contributing \$8.1 billion to the area's overall economy. The city has worked hard to build this component of its economy, which is evidenced by South Texas Medical Center's position as the city's leading employer with almost 26,000 employees. Medical and biomedical fields account for about 14% of the city's jobs. Despite the slowing economy and cutbacks at some companies, the city netted about 10,000 jobs during the past year. Wealth levels remain below the national average. The median household effective buying income, however, continued to trend upward with a 6.3% increase in 2001 to 90.9% of the national level.

Total AV growth slowed in fiscal 2003 due to the economy's general downturn. Growth of 3.1% in fiscal 2003 brought total AV to \$40.8 million. Growth is down compared to the 7% average of the previous five years. H.E. Butt Grocery Co., the leading taxpayer, accounts for just 1.2% of total AV. The city's tax base is well diversified. The 10 leading taxpayers account for just 5.3% of total AV. Tourism and convention traffic continue to be strong as the city experienced an increase in hotel room nights for 2002 following a slight decline after Sept. 11, 2001.

The city's proximity to Mexico promotes strong international trade and tourism, which creates further economic diversity. Air cargo has indicated a strong growth trend, increasing to record levels with continued strong growth projected. Currently, the city's international airport is undergoing expansion and improvements valued at \$425 million.

Government, specifically the military, continues to be a large component of the economy with five military bases in the city. Although Kelly Air Force Base officially closed as a military installation in July 2001, the city has worked on a privatization effort to prevent job losses. To date, 7,000 military jobs have been retained and 5,400 commercial jobs have been created. The city's goal is to create 21,000 jobs at the base by 2006, which would more than offset the estimated 12,000 jobs lost due to the closing. Boeing Co. and Lockheed Martin Corp. are the leading employers at the Kelly installation and are expected to spur further privatization and allow the retention of several aircraft repair operations.

Similarly, the city is working with Brooks Air Force Base to retain jobs there should future base closures be considered nationally. In July 2002, Brooks transferred ownership of all of its land to the city. Part of the city's involvement there includes the development of Brooks Technology & Business Park, where the U.S. Air Force will be the major tenant; the development of additional health services and biotechnology facilities are planned. Brooks City-Base is the only project of its kind in the nation.

San Antonio won its bid for a new Toyota Motor Corp. truck plant, which will be built on land that is south of the downtown area. Construction is scheduled to begin in summer 2003 with completion expected in 2006. The city's economy will benefit from various aspects of the project, including about \$800 million in capital investment from Toyota. The city expects about 2,100 construction jobs to be created, which can be directly attributed to the new Toyota plant. Upon completion, the plant will produce 150,000 of Toyota's Tundra truck annually. The plant is expected to create about 2,000 manufacturing jobs and an additional 5,300 spin-off jobs in the area.

This report was reproduced from Standard & Poor's RatingsDirect, the premier source of real-time, Web-based credit ratings and research from an organization that has been a leader in objective credit analysis for more than 140 years. To preview this dynamic on-line product, visit our RatingsDirect Web site at www.standardandpoors.com/ratingsdirect.
Standard & Poor's.
Setting The Standard.

Published by Standard & Poor's, a Division of The McGraw-Hill Companies, Inc. Executive offices: 1221 Avenue of the Americas, New York, NY 10020. Editorial offices: 55 Water Street, New York, NY 10041. Subscriber services: (1) 212-438-7280. Copyright 2003 by The McGraw-Hill Companies, Inc. Reproduction in whole or in part prohibited except by permission. All rights reserved. Information has been obtained by Standard & Poor's from sources believed to be reliable. However, because of the possibility of human or mechanical error by our sources, Standard & Poor's or others, Standard & Poor's does not guarantee the accuracy, adequacy, or completeness of any information and is not responsible for any errors or omissions or the result obtained from the use of such information. Ratings are statements of opinion, not statements of fact or recommendations to buy, hold, or sell any securities.

The McGraw-Hill Companies